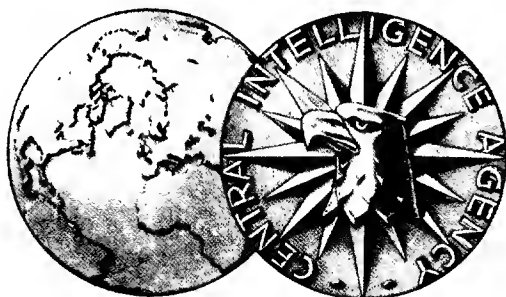


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# REVIEW OF THE WORLD SITUATION



CIA 8-49

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**CENTRAL INTELLIGENCE AGENCY**

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## REVIEW OF THE WORLD SITUATION AS IT RELATES TO THE SECURITY OF THE UNITED STATES

### SUMMARY

1. The Labor Government in the UK has not yet produced a comprehensive policy for meeting a threatening financial-economic trend. The stop-gap measure of cutting dollars imports by 25 percent will have its effects concentrated in North America. There are a few signs that the seriousness of the problem has been felt by the rank-and-file of Labor electorate.

2. The economic condition of Western Germany is developing significant instabilities. Their correction is unlikely except in terms of expanded foreign and domestic trade and extensive long-term credits. The atmosphere in which the federal elections were prepared and took place <sup>was</sup> were unfavorable.

3. The Papal Decree excommunicating Communists has joined battle on a fundamental issue. The ramifications of this conflict can now become complex and widespread. While the Decree will probably not affect the outcome of the Communist attack on the Church in Eastern Europe, it unquestionably brings a very powerful factor into play in the over-all East-West struggle.

4. Yugoslav-Greek relations are in process of changing. No very tangible results have

yet emerged, but the intricate maneuvers between Tito and the Cominform and the West and Tito and the US and the USSR are beginning to have some slight effect.

5. In the Near East, there is little significant change. The new Egyptian coalition government should have a stabilizing effect. Iranian demands for US aid are coming from all quarters within the government, and a lack of coordination is showing.

6. In the Far East, the first proposals for a Pacific Union have undergone change. Most important has been the freezing out of Chiang Kai-shek. The Chinese Communists, still achieving military successes, are running into economic difficulties in large cities and into some peasant resistance in the countryside. The Indonesian problem has good chances of being brought to a reasonably satisfactory conclusion. The Japanese political scene is beginning to boil and the Occupation authorities will be faced with increasingly difficult problems.

7. In Latin America, two areas of instability have developed—Guatemala and Bolivia.

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Note: This review has not been coordinated with the intelligence organizations of the Departments of State, Army, Navy, and the Air Force. The information herein is as of 12 August 1949.

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REVIEW OF THE WORLD SITUATION AS IT RELATES  
TO THE SECURITY OF THE UNITED STATES

## 1. United Kingdom.

No fundamentally curative policy has yet been publicly proposed by the government for checking the increasingly threatening financial-economic trend. There is a likelihood that no such policy has yet been conceived and that neither the government nor the Labor Party is agreed on the basic causes of the crisis or of the action to be taken to meet it. Nothing more fundamental has yet been suggested than to note some remedial measures that might be taken by the US, although it is to be expected that more comprehensive plans will be presented at the Washington Conference in September.

A stop-gap measure, a 25 percent reduction of dollar imports, has been announced. It will be supported by the Commonwealth members of the sterling bloc. Of the six commodities selected for reduction in 1949-50, Canada was the main supplier in 1948-49 of three—timber, paper and wood pulp, and non-ferrous metals. The US was the main supplier of two—raw cotton and tobacco. The sixth item, "dollar" sugar, was largely supplied by Cuba. The effect of the reduction will accordingly be concentrated in North America. The tobacco cuts will probably be passed in part to the British consumer. Soft currency sources exist for maintaining, in considerable part, timber, wood pulp, and non-ferrous metal stocks. It is unlikely, however, that a full 25 percent cut can be made in raw cotton purchases for more than a very short time without injury to the British textile industry. When it is recalled how closely the UK has already restricted its dollar imports to necessities, it is likely that a further cut of this magnitude will, if maintained for long, lead to a lower standard of living, fewer incentives to labor, and specific raw material shortages.

There are few signs, in spite of warnings from the Labor Party and Trade Union leaders, that rank-and-file members recognize and

are prepared to act on the fact of crisis. There have been demands for wage increases, and some threats of strikes. While the notorious Dock Strike arose from other circumstances, its conduct provided an indication of the extent to which the Labor Party leadership is becoming detached from its labor base. An undertone of irresponsibility and defiance is beginning to show among the rank-and-file.

The alternatives in the over-all situation are being defined with increasing sharpness. Short of a marked increase in US loans, grants, or other devices for making dollars available, painful economic and political adjustments within the UK will almost certainly be required. Though Labor has been losing ground politically, it can still be assumed that the Labor Government has enough political strength and authority to call for a considered policy of readjustment. There is, nevertheless, no sign as yet of an agreed intent to do so. No alternative source of political strength and authority has clearly developed in the Conservative Party. The situation remains, therefore, uncertain and subject to sudden interim changes of direction. Prolonged internal uncertainty will have adverse external effects with respect to relations with Western Europe, to the capacity of the UK to maneuver diplomatically, and to the general security position of the US.

## 2. Germany.

Partly for indigenous reasons, and partly in relation to more general economic developments, the Western Zones of Germany are beginning to show signs of instability. The weakening of the economic position has been gradual and its main features now are uncertain employment, reduced sales, and a decline in the production of capital goods. Improvement is unlikely except in connection with an expansion of foreign and domestic trade and the provision of considerable long-term credits. The budget for FY 1949 has

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serious weaknesses. No account is taken of the subsidies needed to stabilize the cost of living; deficiencies in breadgrains, fertilizers, and fodder will require additional imports; and the unanticipated deterioration of the economy of Western Berlin will lead to an added claim. Industrial areas remain in a poor state since capital is not available for rebuilding or for replacing obsolete equipment.

The situation has created an unfavorable atmosphere for the federal elections. The Christian Democrats seem to be losing strength to groups of the Right. This can be partly put down to the identification of the Christian Democrats with a "free-economy" and with the present economic decline. The Socialists are the most likely beneficiaries of this development. Their emergence as the dominant group in a new West German Government would probably result in a trend toward a socialized welfare state, and probable friction with US and particularly French occupation policies. Generally, the new West German Government will be faced with such complex economic and fiscal problems that, regardless of its political color, it will tend to evade responsibility and to blame the Occupying Powers.

The economic situation in Berlin adds nothing except further problems. Unemployment is rising in the western section. One-third of the population exists on marginal incomes drawn from public funds. Industrial activity is handicapped by high production and transportation costs. The municipal budget falls from one point of unbalance to another. Increased personal hardship and lowered morale is almost a certainty as winter sets in.

### 3. The Vatican-Communist Showdown.

The recent Papal Decree excommunicating Catholics who profess, defend, or spread Communism is a final joining of battle on a fundamental issue. The challenge, which has been offered with vigor by the Communist regimes of the Satellite States, has been accepted without reservation by the Holy See. By this decision, the two most powerful organizations for moving men to act on behalf of a doctrine are brought into open and basic conflict. The possible long-term ramifications of this con-

flict cannot be easily or comprehensively defined. The decree will be a very powerful factor in the East-West struggle. In Eastern Europe it implies a struggle to the bitter end; a struggle in which the Communists admittedly have superior material force at their disposal and which they will win; but also a struggle which may possibly result in creating an effective basis for a "resistance movement" in some areas of Eastern Europe. In the West, it clearly defines the lines of battle. In many other areas in the world the decree will exert a powerful and prolonged indirect pressure on both policy and action. Communist governments and Communists generally will have to accept the issue as now posed. Although the Communist governments would obviously have preferred to carry on their anti-church campaign at their own pace, the power of decision has now been taken away from them. The conflict can be pressed on them with a speed and comprehensiveness that may well affect the satisfactory development of other Communist policies.

For the moment, Czechoslovakia is the focal point of the struggle. The Communist technique is, under cover of separating State and Church, to secure control of clerical appointments, education, and Church income. It seeks to do this with the minimum of religious reaction by discrediting the Catholic hierarchy and setting up national Catholic groups with which it can officially deal. The objective of a National Church will certainly be reached, and government control established. In Poland, on the other hand, the issue may be considerably more difficult to handle.

In the West, the immediate point of interest will be Italy. It is considered that the Papal Decree will have definite repercussions in Italian politics. Primarily it will reduce Communist voting strength, but it will also accentuate long-existing clerical and anti-clerical differences.

### 4. Yugoslavia—Greece.

There is little doubt that Tito's policy with respect to Greece and the Greek guerrilla forces is in process of changing. There is also evidence that this change is taking place in the context of growing heat in Tito's relations

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with the Cominform and the USSR. The game is one of very complex maneuvers, delicate balancings, and double-talk; each move taking place in relation to both internal and external factors. The stake is Tito's survival. His main strategy is to avoid final and irrevocable commitment to the West until the West is both able and willing to guarantee the life of his particular regime and thus support his vote as the foremost exponent of "National" versus "Soviet" Communism. Such a guarantee is politically remote.

No very tangible benefits have yet emerged from the sealing of the Greek-Yugoslav border. Neither that action nor the loss of Yugoslav material support will finally check guerrilla effectiveness. The more recent propaganda activities in Macedonia may, however, begin to cut into guerrilla manpower and introduce serious schism into their councils. A considerable guerrilla reaction has developed in the form of violent attacks on Tito as the betrayer of "the cause"; and the situation seems to be producing a genuine lowering of guerrilla morale.

Full implementation by Yugoslavia of a policy of rapprochement with Greece is, however, not yet in sight. At the moment, the policy probably represents little more than a short step acknowledging that there is nothing more to be gained from the guerrilla campaign and that there is danger from the infiltration of pro-Cominform guerrillas into Yugoslav Macedonia. The strength with which longer-range considerations will operate to build up a positive policy of cooperation between the two countries is debatable. The most important of these considerations is probably an estimate of what the West will demand in return for economic concessions.

#### 5. Near East.

The recent formation in Cairo of a coalition cabinet has given Egypt the most representative government in over a decade, strengthened the country's internal stability, and possibly opened a way to better relations with the West. Egypt's major political parties are represented in the new government, which now includes the largest and the opposition party, the WAFD. King Farouk, in engineer-

ing the formation of the present government, may have been motivated by his desire to strengthen his declining prestige both at home and abroad. He was undoubtedly aware of a growing popular demand for a broader-based government, and he may have felt that such a government would improve relations with the UK. Since the new government is more representative, it may be able to deal more effectively with terrorist activities—Communist or Moslem Brothers. Even more important is the probability that it will be able to prepare for reasonably impartial elections. And, though the cabinet—because of its interim nature—may not be able to make actual agreements with the West, it may lay the groundwork for a succeeding government to conclude such accords.

The Iranian Foreign Minister has now added his voice to that of the Prime Minister and the Shah in levying a claim upon the US for direct assistance. The lack of consistency between these various individual official requests suggests at least a lack of coordination, which may in turn seriously delay the execution of much-needed economic measures. It also suggests the possibility that various Iranian leaders are separately developing individual solutions to Iranian problems and aspiring to personal credit for any US aid that may be forthcoming. Certainly the multiplication of proposals reflects uncertainty, anxiety, and dissatisfaction with US attitudes and actions.

#### 6. Far East.

The proposal for a Pacific Union to contain Communism, which was coldly received when co-sponsored in July by Philippine President Quirino and Chiang Kai-shek, may be viewed more favorably by Southeast Asia countries following its revision by Ambassador Carlos P. Romulo, Philippine representative to the UN, and as a result of President Quirino's presentation of the idea in the United States. Romulo, who has now assumed leadership of the project, has apparently persuaded Quirino to drop Chiang from his plans and to place the union on a non-Communist, rather than an anti-Communist basis. The union as presently conceived would be predicated upon the independence of Southeast Asia countries

and dedicated to the maintenance of peace and democracy through political, economic, and cultural cooperation.

It is anticipated that Ambassador Romulo will initiate informal regional consultations perhaps by visits to India and other Southeast Asian countries during August and early September. However, he is unlikely to schedule the anticipated conference of interested nations in the Philippines until after the convening of the UN General Assembly in September, and until the attitude of the US towards the revised proposals is clarified.

The Communist military program in China, which will probably envelop Canton within the month, continues to outrun the political and economic capabilities of the Communist regime. The situation in Shanghai offers an illuminating test case. Local Communist authorities are unable to remedy the economic confusions of a great metropolis. Alternatively, they encourage anti-foreign sentiment and plunder foreign investments, deriving what small and temporary political and economic advantages they can. The US and UK are the principal victims. There is some evidence that the pressure of an unsolved problem is straining both the tempers and the solidarity of the new authorities. In addition, at least for the period of the fall harvests, rural problems will take precedence over the economy of big cities and programs of industrialization. Unpleasant facts exist in the countryside; a growing peasant opposition to Communist methods—in some areas in the form of armed revolts, and a problem of food supplies.

In Indochina, reactions to the newly installed Bao Dai government have ranged from the mildly favorable to the definitely skeptical. The new government has actually accomplished nothing tangible as yet. Official optimistic statements concerning the cooperation of French and Vietnamese troops are not supported by detailed or convincing evidence. The new strategy of operations against Ho Chi Minh, initiated by General Revers, seems impossible of execution unless the French can dispose of a larger contingent of troops than is now available.

An eventual settlement of the Indonesian problem is now within the range of possibility. A cease-fire order has been agreed. The Republic has been able to establish order in its area of responsibility in Central Java. Republican leaders have obtained from the Cabinet and Parliament approval of the agreements entered into with the Netherlands authorities. An accord has apparently been reached with non-Republican groups on the future of Indonesia, and a single agreed position will probably be presented at the Hague Conference. Several developments on the Dutch side also suggest the likelihood of a satisfactory conference. Reactionary Dutch officials have been sidetracked in Batavia. Political and military considerations in the Netherlands make a rapid solution desirable. The doubtful success of the police action and external pressures upon the Netherlands Government work to the same end. The issues that are still unsettled are: the withdrawal of Dutch forces from the archipelago, the degree of autonomy to be exercised by the future Indonesian government, and the control of foreign exchange. These issues are as vexatious as they are vital, but the atmosphere in which they will be taken up will generally be good.

#### 7. The Japanese Political Scene.

The Occupation program has now moved from the establishment of democratic reform to the problem of economic rehabilitation. This problem will naturally be tackled in the political context created by the first stage of Occupation policy. The political context cannot be regarded as very satisfactory. In spite of civil and political reforms, the Japanese people are relatively passive with respect to democracy and its political traditions. Reversion to familiar Japanese patterns will be easy.

Political groupings since the war range from the extreme right (Democratic Liberals) to the extreme left (Communist Party). The Center Groups (Democrats, Socialists, and People's Cooperative) have no sure common ground. The election of January 1949 relegated the Center Groups, which had been the basis of the two previous coalition governments, to the status of a minor opposition group. The partial disintegration of the



power of the Center led to a well-defined polarization in politics, with the major shift of power taking place to the right. The Democratic Liberals now have a firm working majority. The Communists, though relatively weak in comparison, nevertheless made sufficient gains to give them a psychological authority among opposition groups out of all proportion to their numerical strength. The decline of the Center reflects the inability of a string of coalition cabinets to solve economic problems, and an absence of public confidence in the discipline and harmony of a mixed group. More serious is the possible interpretation that, since Occupation policy favored the Center Groups, their collapse represents a vote against the Occupation.

The Democratic Liberal Government, now in possession of political authority, is in the difficult position of being caught between the desires of its constituents, the demands of the Occupation authorities, and the requirements of a presently unviable economy. It will probably proceed by combining a recalcitrant attitude toward SCAP direction, a pronounced anti-Communist tone, and an increasing use of authoritarian controls.

In opposition, the Communists will probably develop several lines simultaneously: nationalism, trade with Communist China, and demands for an early peace treaty. Communist strength is derived from labor, and there is nothing in the economic picture to indicate the sort of improvement that would reduce this support. The present temper of the electorate is not such, however, as to suggest a marked drift to Communism in reaction to repressive measures on the part of the government.

#### 8. Latin America.

The most important developments of the month have occurred in Guatemala and Bolivia. In Guatemala, the assassination of

Colonel Arana removed a moderating and generally pro-US force. An abortive uprising, which followed Arana's murder, was put down by the Arévalo Government which used, in addition to regulars, armed civilian leftist groups for the purpose. The government's local stability and its leftist orientation have both been strengthened. The Arévalo Government uses Communist sympathizers in important positions, has shown itself distinctly unfriendly to US business interests, has aggravated the question of European dependencies in the Western Hemisphere, and has disturbed Caribbean affairs by aiding the revolutionary attempt against the Dominican Republic. While the government certainly does not have the ability—and probably does not have even the inclination—to side with the USSR in an actual conflict, it will probably continue and may intensify its opposition to certain US policies during the present "cold-war" period.

In Bolivia, it has recently been reported that an agreement has been signed between the MNR (Movimiento Nacional Revolucionario) and the PIR (Partido de la Izquierda Revolucionaria). The former is strongly nationalist, authoritarian, and generally anti-US; the latter, in which the Communists have recently extended their control, has a party line that does not now differ in any important degree from orthodox Moscow doctrine. These two groups control Bolivian labor and have considerable influence within the country. They are to some extent unnatural allies, but they are quite capable of maintaining a common front until the present government—which depends on a slim congressional majority and the not too reliable support of the Bolivian Army—is overthrown. The government will be able to maintain itself against this strong opposition only if it finds means to ensure economic stability and to retain the loyalty of the armed forces. Its own resources may be insufficient to provide these means.

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